DOCUMENT RESUME

ED 406 528 CE 073 739

TITLE	Employment Training Panel: Has Achieved Many of Its Training Program Responsibilities Despite Some Administrative and Planning Problems.
INSTITUTION	California State Office of the Auditor General, Sacramento.
PUB DATE	Oct 96
NOTE	38p.
AVAILABLE FROM	California State Auditor, Bureau of State Audits, 660 J Street, Suite 300, Sacramento, CA 95814 ($5).
PUB TYPE	Reports - Evaluative (142)
EDRS PRICE	MF01/PC02 Plus Postage.
DESCRIPTORS	Agency Role; *Audits (Verification); Contracts; *Job Training; *Program Administration; Program Effectiveness; *State Agencies; *State Programs; Strategic Planning
IDENTIFIERS	*California Employment Training Panel

ABSTRACT

California's Employment Training Panel was created in 1982 to work in partnership with the state's businesses, labor unions, and government to provide training funds to California businesses. In 1995, the Employment Training Panel's administrative practices, strategic planning efforts, and contracting policies and practices/procedures were reviewed through an audit process that included interviews with panel executives and other key staff and a review of a sample of 15 contracts awarded during fiscal years 1993-94 through 1995-96 and a sample of internal contracts. The panel was found to be handling many of its contracting and administrative responsibilities well; however, several problems/areas requiring improvement were identified. Among the audit's conclusions were the following: the panel inappropriately used a training contract to earmark $7 million for a specific group; the panel may be extending inappropriately the period for which funds are available to it and may be exceeding its administrative cap; the panel could improve its strategic planning efforts; and it should estimate training contract amounts more accurately. The panel generally concurred with the audit findings and agreed that improvements can be made in several areas as identified in the audit report. (MN)

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Has Achieved Many of Its Training Program Responsibilities Despite Some Administrative and Planning Problems

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CALIFORNIA STATE AUDITOR

KURT R. SJOBERG
STATE AUDITOR

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October 1, 1996 96023

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As required by Chapter 865, Statutes of 1995, the Bureau of State Audits presents its audit report concerning the Employment Training Panel's (panel) contracting and administrative practices. This report concludes that the panel has achieved many of its training program responsibilities despite some administrative and planning problems. Specifically, we found that the panel accomplishes many of its program and administrative responsibilities. However, the panel could improve its strategic planning by stating its objectives in measurable terms and establishing performance benchmarks for its employees. Additionally, the panel needs to better estimate the amount of money its training contractors will earn each year, as the amounts that remain unspent are excessive. Finally, the panel has engaged in certain administrative practices that, although legal, appear to be improper, including extending the life of its appropriated funds, expending more than 15 percent of appropriated funds on administration, and encumbering funds to a contract from which the panel received no training services.

Respectfully submitted,

KURT R. SJOBERG
State Auditor

Employment Training Panel:

Has Achieved Many of Its Training Program Responsibilities Despite Some Administrative and Planning Problems

October 1996
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CALIFORNIA STATE AUDITOR

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Summary

Audit Highlights . . .

The Employment Training Panel is handling many of its contracting and administrative responsibilities well.

However, it:

- ☑ ***Could improve its strategic planning efforts.***
- ☑ ***Needs to estimate training contract amounts more accurately.***
- ☑ ***May be inappropriately extending the amount of time funds are available to it, and exceeding its administrative cap.***
- ☑ ***Inappropriately used a training contract to earmark $7 million for a specific group.***

Results in Brief

The Employment Training Panel (panel) was originally created in 1982 to provide training funds to California businesses. The panel works in partnership with business, labor, and government to provide funds for training California's workforce in the skills necessary for businesses to remain viable and to compete in the global economy while providing workers with reasonable wages and secure employment.

Our review focused on the panel's administrative practices, its strategic planning efforts, and its contracting policies, procedures, and practices. During our review, we found:

- The panel is accomplishing many of its responsibilities. Specifically, it has issued contracts to only those companies eligible to receive training funds, developed a plan to adequately address a backlog of audits, and properly followed up on funds paid to, but not earned by, contractors. Additionally, the purposes of the panel's administrative contracts were reasonable; the processes the panel used to develop, implement, and communicate its directives, policies, and procedures were sensible; and its electronic data processing system is generally accurate.

- The panel could improve its strategic planning efforts by stating its goals and objectives in measurable terms and identifying performance benchmarks for its employees. Although it identifies in its strategic plan several goals and objectives that are congruous with its mission, the panel has not stated them in measurable terms. Additionally, while most of its units produce reports that indicate their level of performance, they do not establish benchmarks against which they could evaluate employees' success in achieving goals and objectives. As a result, the panel is unable to impartially determine whether it and its employees successfully accomplish its goals and objectives and, therefore, fulfill its mission.

- The panel needs to better estimate the amount of money its training contractors will earn each year, as the amounts that remain unspent are excessive. During fiscal years 1992-93 through 1994-95, contractors did not earn, and the panel was forced to disencumber or rescind, an average of 42 percent of the funds it had awarded for training contracts. As a result, the panel unnecessarily tied up funds it could have provided to other contractors.

- Some panel fiscal practices may not be appropriate. Specifically, by using a provision in the annual budget act that allows it to change prior-year appropriated funds into current-year funds, the panel may be inappropriately extending the amount of time funds are available to it. Additionally, because the Unemployment Insurance Code allows it to spend on its administration up to 15 percent of funds appropriated by the Legislature for a fiscal year plus up to 15 percent of those funds it disencumbers from prior fiscal years, the panel may be spending more than intended for administrative expenses.

- The panel inappropriately encumbered $7 million for a contract from which it never intended to receive or pay for training services. During fiscal year 1993-94, the panel entered into a training contract with the California Manufacturers Association (CMA) for $7 million. However, it never intended the CMA to provide training services. Rather, the CMA was to develop, or market, potential projects from among CMA membership. Effectively, the panel earmarked $7 million in training funds for CMA members by encumbering these funds in the contract. As a result, it unnecessarily made some contractors wait for training funds, avoided reverting $2.9 million to the Unemployment Insurance Fund as required by the Unemployment Insurance Code, and wasted the time of its staff members, and the staff at the Employment Development Department who handle the panel's accounting function.

Recommendations

To ensure that it is successful in achieving its stated goals and objectives and fulfilling its mission, the panel should modify its strategic plan, stating its organizational goals and objectives in measurable terms whenever possible. Additionally, the panel

should establish benchmarks for key performance indicators for its employees to measure their success and challenge their performance.

To more effectively manage the distribution of training funds, the panel needs to more accurately calculate training contract awards. In addition, the panel should include in its annual report the effect of implementing recommendations from the disencumbrance report. If the changes made are not effective in reducing disencumbrances, the panel should consider alternative means to better manage training funds, such as using phased contracts, imposing a penalty on unsuccessful companies, or other suggestions from the Advisory Research Council or the California State University, Northridge.

To ensure the panel is spending its funds appropriately, the Legislature should consider the methods by which the panel is able to extend the life of its appropriated funds, and, if contrary to legislative intent, eliminate the budget act language allowing it to re-encumber funds. Further, the Legislature should consider the methods employed by the panel to use more than 15 percent of appropriated funds for administration, and if contrary to the intent of the Legislature, limit administrative costs to a certain percentage of funds appropriated each year excluding amounts disencumbered from prior fiscal year appropriations.

To improve the effectiveness and propriety of its operations, the panel should stop entering into contracts and encumbering training funds for which contractors do not intend to provide training services.

Agency Comments

The panel generally concurs with the findings and agrees that improvements can be made in several areas as identified in the audit report. In addition, the panel noted that it has already begun to address some of our recommendations. With regard to the issue of some fiscal practices being inappropriate, the panel believes that the Legislature did intend for the panel to have the ability to prolong the availability of funds beyond three years. Finally, the panel believes that the Unemployment Insurance Code allows it to include funds disencumbered from prior years when determining the amount it can spend on administrative costs.

Introduction

Background

The Employment Training Panel (panel) was originally created in 1982 to assist employers in jeopardy of laying off workers or in need of skilled employees to work with new technologies. The panel provided funding to train employees in the use of new technologies, which, in turn, provided the employers with operating efficiencies. Effective January 1, 1994, legislation required the panel to focus on projects that benefit the California economy as a whole, rather than individual entities, by funding contracts that retrain workers in companies challenged by out-of-state competition.

The panel consists of eight members who have backgrounds in business, management, labor, or employee relations. The governor appoints three members, including the chairman, while the Senate and Assembly each appoint two members. The eighth member, either the Secretary of the Trade and Commerce Agency or his or her designee, serves as an ex officio voting member. The panel's headquarters is located in Sacramento, and it has field offices in Sacramento, San Mateo, Los Angeles, and San Diego. The administrative head is the executive director, who oversees approximately 128 employees. The panel is funded through a one-tenth of one percent tax imposed on employers subject to the unemployment insurance tax of California.

The California Unemployment Insurance Code directs the panel to fund only those training projects that do the following:

- Foster creation of high-wage, high-skilled jobs or retention of high-wage, high-skilled jobs that are threatened by out-of-state competition.

- Encourage industry-based investment in human resource development that promotes the competitiveness of California industry through productivity and product quality enhancements.

- Result in secure jobs for those who successfully complete training.

- Supplement rather than displace funds available from other programs.

During fiscal year 1995-96, the panel entered into 226 training contracts totaling $48.8 million. Most of the projects it funds are to train new, recently employed, or incumbent workers of companies locating to or expanding operations in California, and to maintain the viability of current businesses. Contracts may extend for up to two years, and reimbursement is contingent upon successful contractor performance.

These performance-based contracts require contractors to provide the agreed training, and require the employers to pay the minimum wage established in the contract and retain the trainee as an employee for a period of at least 90 days after the training is complete, to be reimbursed. When it enters into a contract with a company to provide training, the panel allocates, or encumbers, the total amount from the funds available through its annual appropriation from the State. This encumbrance reserves the funds so that the panel can pay the contractor if the contracting organization provides training that complies with applicable contract terms. If the contractor is not able to provide the training or does not provide a training program that meets the contract terms, the panel does not pay, but rather rescinds, or disencumbers, these funds. It may then commit the disencumbered funds to other contracts.

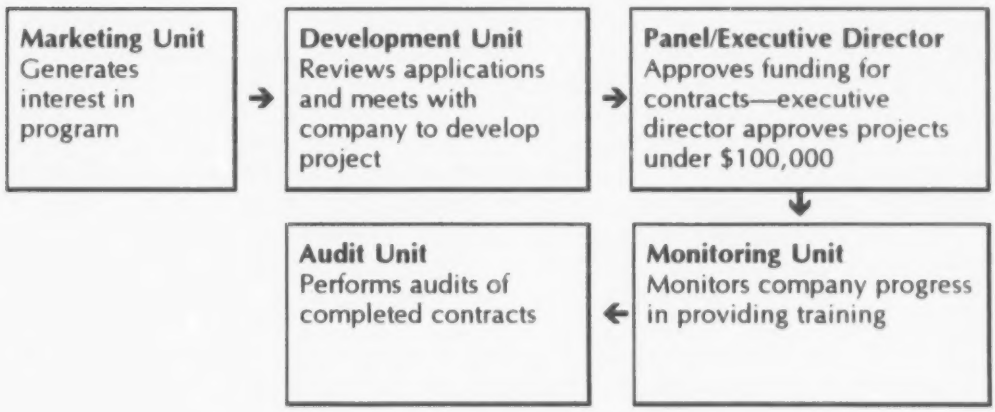
The Panel's Contracting Process

To disburse training funds, the panel follows a contracting process that involves multiple units within the panel. Figure 1 on page 3 depicts this process. It begins with the marketing unit generating interest in the panel's program and purpose. To inform eligible companies about the program and the funds available to them, the marketing unit works with the California Trade and Commerce Agency, which has an interagency agreement to perform marketing services for the panel. The California Trade and Commerce Agency has four regional marketing representatives throughout the State who work with the panel to apprise California businesses of the funding program and assist those businesses in submitting applications. A company wishing to receive panel funds must submit an application to the headquarters in Sacramento. Headquarters' staff perform an initial review to ensure that the application is complete and then assign it to one of the four regional offices.

At the regional office, staff in one of the panel's development units work with the company to prepare a proposed agreement. Additionally, companies sometimes use the services of an outside consultant to help them complete their application, develop a proposed agreement, and administer their training program. When a proposed agreement is complete, the eight-member panel or the executive director evaluates it for possible approval. Currently, the executive director has discretion to approve most proposed agreements valued at $100,000 or less. The eight-member panel approves contracts over $100,000. When a proposed agreement receives approval, it becomes a contract. Once signed, one of the two monitoring units oversees the activities of the contractor to ensure compliance with the terms of the contract. In addition, the panel's audit unit performs reviews of selected contracts after they are completed to ensure that contractors provided training in accordance with the terms of the contract.

Figure 1

Employment Training Panel Contracting Process


Marketing Unit
Generates interest in program
Development Unit
Reviews applications and meets with company to develop project
Panel/Executive Director
Approves funding for contracts—executive director approves projects under $100,000
Monitoring Unit
Monitors company progress in providing training
Audit Unit
Performs audits of completed contracts

Other Related Reviews of the Panel Currently Under Way

In addition to our review, two other entities are currently reviewing the panel's operations. The panel has assembled the Advisory Research Council, consisting of panel members and individuals from labor, management, and industry, who will issue a report to the Legislature by December 31, 1996, on

ways the panel can improve its process of preparing, funding, and implementing contracts. Additionally, the panel has entered into an interagency agreement with California State University, Northridge, to study the effects the contractors' use of consultants has on the success of contracts. As described in the following section, we limited the scope of our audit in these areas so that we did not duplicate the efforts of these other reviews.

Scope and Methodology

Chapter 865, Statutes of 1995, directed the Bureau of State Audits to conduct a comprehensive management review and evaluation of the panel. This legislation directed that we include the following issues in our review:

- The panel's contracting policies, procedures, and regulations;
- The panel's decision making processes for contracts;
- The cost and efficiency of the administration of internal panel contracts;
- The methods and procedures involved in setting the panel's internal administrative and procedural regulations; and
- The internal administrative policies and procedures of the panel.

In addition to evaluating these issues, we determined whether the panel had established mission statements, identified goals and objectives, and developed workload standards for its various units. To accomplish this, we interviewed panel executives and other key staff. We also reviewed its most recent strategic plan to determine whether the plan identified goals and objectives, action plans, and time lines management could use as guides in accomplishing the panel's overall mission.

To assess contracting policies, procedures, and regulations, we interviewed panel staff and identified the activities of the application review, contract development, monitoring, and audit units. Further, we determined whether any other entities had performed or were currently performing related reviews. We determined that two reviews currently underway address the panel's contract processes. As discussed in the previous

section, the Advisory Research Council and California State University, Northridge, are evaluating the panel's contracting practices. The Advisory Research Council is reviewing the panel's processes, policies, and regulations related to preparing, funding, and implementing training contracts. California State University, Northridge, is studying the effect the contractors' use of consultants has on the success of training contracts. Therefore, our audit did not include a review of these areas. However, we did evaluate the activities of the panel's audit unit. Specifically, to determine if they were reasonable and appropriate, we assessed the unit's audit sampling techniques and its plan to retire a backlog of audits accumulated at June 30, 1996.

To assess its process for approving and awarding contracts, we interviewed key panel staff. We selected a sample of 15 contracts awarded during fiscal years 1993-94 through 1995-96 to determine if each contractor was eligible to receive panel funds.

To evaluate the efficiency of administration of internal, or non-training, panel contracts, we reviewed a sample of internal contracts and determined whether the nature of the services or goods received was reasonable.

To assess the methods and procedures involved in setting internal administrative and procedural directives, we interviewed key panel staff and learned how the panel develops its administrative and procedural directives.

Chapter

The Panel Achieves Many of Its Responsibilities; However, It Could Improve Its Administration and Planning

Chapter Summary

The mission of the Employment Training Panel (panel) is to work in partnership with business, labor, and government to provide funds for training California's workforce in the skills necessary for businesses to remain viable and to compete in the global economy while providing workers with reasonable wages and secure employment. Our review of several of the panel's operations revealed no significant problems in its efforts to fulfill this mission. For example, we found that the panel issued contracts only to those companies eligible to receive training funds, developed a plan to adequately address a backlog of training contractor audits, and adequately followed up on funds paid to, but not earned by, contractors. Additionally, the purposes of the panel's administrative contracts were reasonable. Moreover, the processes it used to develop, implement, and communicate its directives, policies, and procedures were sensible. Finally, the panel's electronic data processing system is generally accurate.

Although we found no significant problems to report in the areas described above, the panel could improve its strategic planning efforts and its process for estimating amounts contractors will earn. First, the panel needs to complete its strategic planning efforts. Although it has defined its vision and mission statements and established goals and objectives to fulfill this mission, the panel has not stated them in measurable terms. Furthermore, some units have not set benchmarks against which they can evaluate their employees' success. Because the panel did not state its goals and objectives in measurable terms, and because several of its units have not identified benchmarks for their employees, the panel cannot determine impartially whether it is successfully accomplishing its goals and objectives and thus fulfilling its mission.

Second, the panel could improve the way it determines how much money its training contractors will be able to earn each year. Specifically, the panel needs to better estimate and monitor the amount of funds it dedicates to individual

contractors, as the amounts that remain unspent are excessive. During fiscal years 1992-93 through 1994-95, contractors did not earn, and the panel was forced to disencumber or rescind, an average of 42 percent of the funds it had awarded for training contracts. For example, the panel disencumbered, or rescinded, $38 million (41 percent) of the $93 million it awarded in fiscal year 1993-94 because contractors did not provide the necessary training to fully earn the amount of funds allocated to them. As a result, the panel unnecessarily tied up funds it could have provided to other contractors.

Finally, we identified some fiscal practices that may not be appropriate. First, by using a provision in the annual budget act, the panel is able to extend the amount of time funds are available to it by disencumbering and then immediately re-encumbering them. Second, because the Unemployment Insurance Code allows it to spend on administration up to 15 percent of funds appropriated to it by the Legislature for a fiscal year plus up to 15 percent of those funds it disencumbers from prior fiscal years, the panel may be spending more than intended for administrative expenses. Finally, the panel inappropriately encumbered $7 million to a training contract from which it never intended to receive or pay for training services. As a result, some contractors had to unnecessarily wait for funding, the panel kept $2.9 million that should have reverted to the Unemployment Insurance Fund, and panel staff, as well as staff at the Employment Development Department, wasted contract and fiscal management efforts.

The Panel Is Accomplishing Many of Its Responsibilities but Can Improve Its Strategic Planning Process

The panel is accomplishing its responsibilities in many of the areas we reviewed. Specifically, we analyzed efforts in several program and administrative areas for providing training funds to eligible companies and found the panel was fulfilling many of its responsibilities. However, it could better state the goals and objectives listed in its strategic plan and identify benchmarks for its employees. In doing so, the panel could determine objectively whether it is successful in fulfilling its mission.

The Panel Is Fulfilling Its Responsibilities in Program Areas

The panel is meeting many of its responsibilities related to funding training programs. For example, the panel adequately carried out its duties for ensuring that it issued contracts to only eligible companies. We reviewed a sample of 5 contracts the panel entered into for each of the last three fiscal years to determine if the companies receiving funds met the eligibility requirements established in the Unemployment Insurance Code. For all 15 contracts, the contractors met minimum eligibility standards.

The panel has issued contracts only to eligible companies, has developed a plan to eliminate its audit backlog, and has followed established procedures to collect amounts due.

Additionally, the panel developed a plan to adequately address a backlog of training contract audits over the next three years. Before fiscal year 1995-96, it entered into an agreement with the Employment Development Department to audit completed contracts. In fiscal year 1995-96, using its own audit unit, the panel began performing these audits; however, due to staff shortages and the initial training of new auditors, it was not able to complete by June 30, 1996, 35 of the 47 audits it planned for fiscal year 1995-96. However, for 14 of these 35 audits, the panel had completed its audit fieldwork and only needed to issue a report. We reviewed the approved plan and determined that it appears to reasonably and adequately eliminate the backlog.

Finally, the panel properly followed up on funds paid to, but not earned by, contractors. Most of these receivables resulted from the panel making advance payments to contractors and later determining, through its monitoring or audit functions, that the contractor did not earn the amount paid. We reviewed nine contracts for which the contractor owed the panel and found that it followed established collection procedures or was actively pursuing the amounts due. Despite its best efforts, however, the panel has been unsuccessful in collecting the amounts due for many of the contracts it overpaid. Specifically, during fiscal year 1995-96, contractors owed an average of $7.8 million. During this period, the panel only collected $370,000. For $5.1 million (65 percent) of the $7.8 million owed at June 30, 1996, the panel had exhausted its avenues for recovering the funds. These accounts are currently being processed through the Board of Control as uncollectable, are in bankruptcy, or have been referred to the Attorney General's Office for legal action.

The Panel Is Fulfilling Its Duties in Administrative Areas

In many administrative areas, the panel is also accomplishing its responsibilities. For example, the methods it uses to identify issues and obtain information before establishing policies are reasonable and appropriate. In addition, the panel's non-training contracts involved services and goods that appeared appropriate and necessary for the panel to accomplish its mission.

Furthermore, the panel's electronic data-processing system is generally accurate. Specifically, we reviewed a total of 60 projects approved during fiscal years 1994-95 and 1995-96 by comparing key information contained in the system to supporting documents in the panel's contract files. Although we found minor inaccuracies in the data and other minor weaknesses in the system, these errors did not materially affect the integrity of the information maintained by the data-processing system.

The Panel Could Improve Its Strategic Planning Efforts

As part of our audit of operations, we reviewed the panel's effort to adopt and implement a strategic plan. Although it has established both a vision and a mission statement for its organization, the objectives identified to fulfill its mission are not stated in measurable terms. Furthermore, the panel has not established performance benchmarks for some of its employees.

Strategic planning is a long-term, future-oriented process of assessment, goal setting, and decision making that maps an explicit path between the present and a vision for the future. Essential elements of sound strategic planning include the following:

- Analyzing the work environment to identify strengths, weaknesses, problems, and opportunities;
- Identifying key issues relating to the organization's mission and planned activities;
- Defining the mission and formulating consistent goals;
- Establishing priorities among the goals and allocating resources accordingly;

- Defining the objectives necessary to achieve each stated goal;

- Establishing time lines and action plans to complete each objective;

- Defining benchmarks or targets for each significant activity; and

- Measuring the results of planned operations against the benchmarks to evaluate performance and reset targets as necessary.

Successful planning efforts provide many benefits both to an agency and to the clients it serves. For example, strategic planning will improve an agency's ability to anticipate and accommodate the future by identifying its issues, opportunities, and problems. Because it focuses on results, good strategic planning will enhance decision making at both the operational and executive levels. Planning efforts geared towards outcomes or benefits also explicitly emphasize client satisfaction. Successful strategic planning provides needed information to guide managers in making resource allocation decisions and establishes a basis for measuring the success of the agency's activities.

The fundamental concept underlying strategic planning is its dynamic nature. The planning process is not a one-time project that the organization completes. Strategic planning should be an iterative process that an agency refines and refocuses as the agency measures performance, resets targets, and gathers new information.

Although the objectives identified in the panel's strategic plan are consistent with its mission, they are not stated in terms that can be measured or benchmarked.

In its strategic plan, the panel has established both a vision and a mission statement for its organization. The plan identifies the strategies and objectives the panel will employ to fulfill its stated mission. Additionally, each unit has a stated mission that is congruous with the panel's overall mission. The methods and objectives the panel has identified in its current strategic plan are also consistent with its mission statement.

However, the objectives are not stated in measurable terms so that the panel can determine its success after the planning period is over. For example, one objective the panel includes in its current strategic plan is "ongoing introduction of the (panel) program to the public and provision of technical assistance prior to contract development." The plan goes on to explain that the panel will increase efforts to ensure that contractors have better up-front knowledge of all training

options and requirements to improve their training projects' chances for success. However, the panel has not identified how it will measure whether it is achieving this objective and, therefore, is unable to determine its success. As a result, the panel is unable to ascertain whether it needs to modify its strategies for fulfilling its mission.

Additionally, we reviewed 5 of the panel's 11 units to determine if each is identifying performance indicators, such as benchmarks, time lines, or workload standards, and whether it is using the indicators to evaluate unit and employee effectiveness in achieving the unit's stated mission. While most of them had reports that showed the activities and production output, the units often had not identified, or did not use, benchmarks or standards against which their employees could be evaluated. Of the five managers we interviewed, three stated that, although they reviewed activity reports at least monthly, they had not established, or did not use, performance benchmarks to determine whether employees were performing adequately.

The Panel Needs To Better Manage Its Distribution of Funds

During our review, we noted areas in which the panel could improve its operating effectiveness and efficiency. Specifically, it could better estimate the funds each contractor will earn, thereby making funds available to more contractors than it does currently. Further, the panel needs to improve some of its fund management practices.

The Panel Needs To Better Estimate the Amount of Funds Contractors Will Earn

The panel needs to develop better estimates of the amounts its contractors will earn so that it can increase the number of contractors it serves in a particular fiscal year. By increasing the number of contractors, the positive impact training funds will have on the State's economy may occur earlier than if some contractors wait to receive funds. In addition, more accurate estimates of contractors' funding needs would lower the rate of disencumbrances the panel incurs each year.

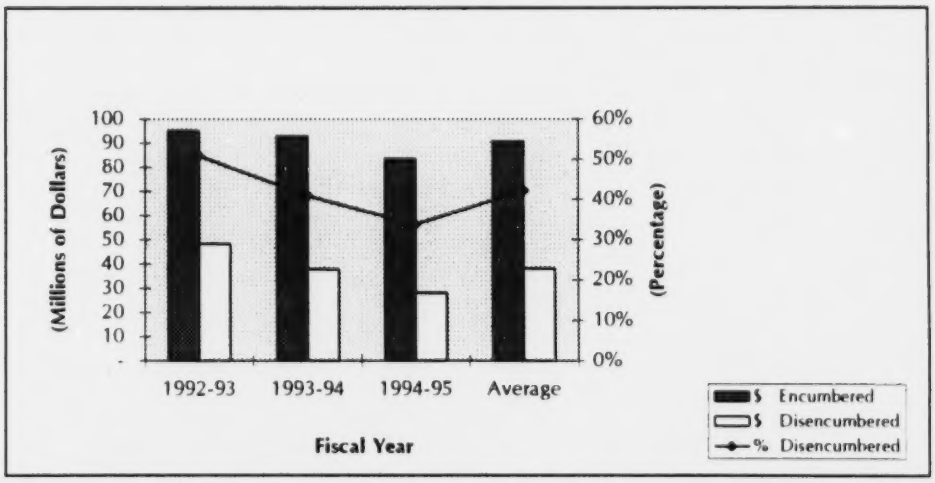
When it does not accurately estimate the amount of funds a contractor will earn and awards too much money, the panel may force other contractors to wait for funds to train their employees. This delay then postpones the training funds' effect on the State's economy. For example, if we assume that demand for panel funds exceeds funds available for fiscal year 1996-97, some contractors must wait until the panel receives additional funds in fiscal year 1997-98 and delay employee training. If the panel better estimated amounts required for contracts, it would be able to fund these delayed contracts sooner, thus minimizing the time required for panel funds to impact the State's economy.

The panel rescinded 42 percent of the $90.6 million it awarded.

We reviewed disencumbrances for funds originally contracted during fiscal years 1992-93, 1993-94, and 1994-95, and found that the rate at which the panel disencumbered or rescinded money from individual contracts was exceedingly high. As Figure 2 below indicates, the panel disencumbered an average of $38.2 million, or 42 percent, of the $90.6 million it awarded for training contracts during these years. Even though the panel's disencumbrance rate has been decreasing, we estimate that it will still disencumber $28.3 million (34 percent) of the $83.6 million it awarded in fiscal year 1994-95.

Figure 2

Panel Disencumbrances



Although it subsequently commits disencumbered funds to other training contracts, this high rate of disencumbrances adversely affects the panel's program. When it disencumbers training

funds and then awards them to a different contractor, the impact of those funds on the State's economy is delayed. The panel disencumbers most of the funds in question during the second year after contract approval. Therefore, if it entered into a contract in fiscal year 1994-95, most of the unearned funds from that contract will be disencumbered during fiscal year 1996-97. It will encumber the unearned funds to another contract, whose term will likely extend from fiscal year 1996-97 through 1998-99. Even though the funds are re-encumbered in 1996-97, they may not actually be spent until the end of the new contract period. As a result, funds the panel originally encumbered in fiscal year 1994-95 would not be spent until four years later, delaying the positive impact the training funds may have on the State's economy. While the above example assumes that all of the money re-encumbered in fiscal year 1996-97 will be earned by and paid to the contractor, past history indicates that, on average, 42 percent of the panel's contract amounts are later disencumbered; therefore, a portion of these funds would again be disencumbered and re-encumbered to another new contract. This process could go on for several years, further postponing the impact on the State's economy of the appropriation the panel received in fiscal year 1994-95.

When training contracts are overfunded, the benefits to the State's economy from the unspent funds are delayed.

By Revising Its Contract Management Practices, the Panel Could Serve Employers Sooner

In an effort to improve its program operations, the panel's planning and research unit conducted a study to determine the major causes of disencumbrances in training contracts and make recommendations for reducing them. In May 1995, the planning and research unit issued a report based on the study identifying eight factors that influence disencumbrances:

The panel could reduce the amount of unspent training funds by addressing eight influential factors.

- Larger contracts tend to have larger disencumbrance rates.
- Contracts without amendments have higher disencumbrance rates than those with amendments.
- Service industries have higher disencumbrance rates than manufacturing.
- Newer businesses (less than ten years old) have higher disencumbrance rates than established businesses.

- Contractors that use subcontractors have higher disencumbrance rates than those that do not.

- Contracts that include structured on-site training have higher disencumbrance rates than those that do not.

- Contracts with more than 200 hours of training per trainee have higher disencumbrance rates than those with fewer hours.

- Lack of panel administrative oversight in the early phases of a contract results in higher disencumbrances.

The report also included six specific recommendations for reducing disencumbrances and acknowledged that the panel is not able to control some of the factors affecting the disencumbrance rate. Therefore, the panel may never be able to reduce its disencumbrances to zero. However, the report did state, and we agree, that the panel could lower the rate of disencumbrances by addressing those causes it can control.

The panel has implemented four of these six recommendations. Specifically, it streamlined the original amendment process so the contractor can more easily amend its contract after execution if the need arises. In addition, the panel's development analysts now review proposed agreements, and identify and include in the package for approval the following risk indicators for all retraining contracts:

- Contractors with previous contracts that resulted in large disencumbrances;

- Proposals that include subcontractors that will perform administrative duties;

- Contractors with more than 250 employees;

- Training projects in the services industry;

- Contractors in business ten years or less;

- Proposals that include subcontractors for training, or for training and administration;

- Proposals for more than 200 training hours per trainee; and

- Proposals that include structured on-site training.

To simplify structured on-site training contracts, the panel revised its documentation requirements.

In response to another recommendation, during fiscal year 1996-97, the panel revised documentation requirements with which contractors must comply to be reimbursed for structured on-site training. Under the new requirements, rather than documenting the amount of structured on-site training each trainee receives, each contractor must report the number of hours its trainer spends with trainees and certify that each employee the contractor claims as trained has attained competency as specified by the curriculum.

The final recommendation the panel implemented was establishing a control to determine whether a contractor is making progress. Approximately 30 days after the start of training, analysts conduct the first monitoring site visit. A typical site visit includes a review of program status, observation of training, trainer and trainee interviews, and a review of trainee records. The monitors normally conduct subsequent visits on a quarterly basis. If they identify projects for which no activity has occurred within six months after start-up, the monitors will offer immediate technical assistance to help initiate project activity. If no subsequent activity occurs within an additional three months, the monitor will terminate the project.

Because disencumbrances often do not occur until two years after the panel awards a contract, and because the panel implemented these recommendations during fiscal years 1995-96 and 1996-97, we were unable to determine the effect of the changes on the rate of disencumbrances. However, the panel should begin to see their effects by the end of fiscal year 1996-97, and to a greater extent by the end of fiscal year 1997-98. Finally, although it takes up to two years for most unearned funds to be disencumbered, the changes should lower the panel's disencumbrance rate to a limited degree.

The panel has not implemented two of the six recommendations made in the disencumbrance report: implementing projects in phases and involving contractors in the administration of their own contracts. According to the executive director, the panel has not implemented contract phasing because of concerns raised by the Employment Development Department and the Department of Finance about making commitments for future years without placing funds aside. The executive director also stated that the panel's concerns regarding increased administrative workloads inhibited further consideration of contract phasing. He further stated that streamlining the amendment process by which a contractor increases or decreases the funding in a contract should reduce the tendency of contractors to ask initially for more money than they can realistically use.

The panel has implemented several measures to better manage its training contracts.

The panel has already taken some measures to get the contractors' management involved in the administration of training programs. For example, it requires contractors to have one of their senior management representatives present at initial planning meetings. However, according to its executive director, the panel is not legally able to mandate that contractors manage their own training program administration or curricula and cannot prevent them from choosing to use subcontractors for these purposes.

The Unemployment Insurance Code, Section 10205(g), requires the panel to evaluate the effectiveness of its training programs. In fulfilling this requirement, the panel entered into an interagency agreement with California State University, Northridge, to study the role of consultants in contracts. California State University, Northridge, will present its findings in December 1996. The panel should then submit these findings to the Legislature along with its plans to further involve contractor management in contract administration and performance.

The Panel Could Adopt Policies To Deter Contractors From Overstating Their Funding Needs

In addition to more closely estimating contract amounts, the panel could adopt measures that would discourage a contractor from requesting more training funds than it needs. The panel later disencumbers these excess funds when it determines the contractor will not be able to earn them. If it were to adopt policies that would deter contractors from overstating their needs, the panel could reduce disencumbrances.

One way the panel could encourage contractors to make realistic funding requests would be to adopt a policy of penalizing those that do not successfully complete their contracts. For example, if a contractor does not successfully complete all the training for which it contracted, the panel would fund the completed training at a reduced rate. This would provide a fiscal incentive to the contractor to accomplish all the training planned and a disincentive to request more funds than necessary. In those instances in which a contractor earns no panel funds, and therefore the panel cannot reduce the amount otherwise funded, this option may not be possible. However, as indicated in Table 1, according to the panel's disencumbrance report based on fiscal year 1993-94 data, only 9.8 percent of the contracts resulted in 100 percent

disencumbrances. Therefore, this proposed policy would affect most contractors that do not complete the training outlined in their contracts.

Table 1

Success Rates of Fiscal Year 1993-94 Panel Contracts

Percentage of Contract Amount Earned	Number of Contracts	Percentage of Total Contracts	Total Amount Disencumbered
100%	18	8.8%	$ 0
90 - 99	24	11.7	277,000
80 - 89	33	16.1	864,000
70 - 79	30	14.6	2,569,000
60 - 69	13	6.3	1,532,000
50 - 59	16	7.8	2,526,000
1 - 49	51	24.9	18,712,000
0	20	9.8	4,345,000
Totals	**205**	**100%**	$30,825,000

Some Panel Fiscal Practices May Not Be Appropriate

During our review of the panel's fund allocation and disencumbrance processes, we identified a practice that may not be appropriate. This practice extends the life of the panel's fiscal appropriations. In fiscal year 1985-86, the Legislature changed the length of time for which funds were appropriated, or made available, to the panel from a "continuous appropriation" to an appropriation that is available for three years. Continuous appropriations allowed funds to remain available for use without regard to the fiscal year. Therefore, funds appropriated to the panel in a certain fiscal year not encumbered or spent by the end of that year would roll over to the next fiscal year and be available for other projects. Under the 1985-86 legislation, appropriations available for three years must be encumbered in the first year and spent within the next two years. If it does not spend the funds within these time frames, they revert to the originating fund. By changing the length of time it has to use its appropriation, the Legislature effectively forced the panel to be more accountable for its funds.

Although the Legislature appropriates training funds for only three years, the panel's practice of reallocating unspent funds extends this by at least two additional years.

However, a provision in the annual budget act permits the panel to reallocate funds that it has disencumbered from prior-year training contracts. This provision allows the panel to change prior-year appropriated funds into current-year funds. For example, assume the panel encumbers $100,000 to a contract in fiscal year 1994-95 using funds appropriated in that year. In fiscal year 1996-97, it determines that the contractor will not be able to earn $25,000 of the contract amount. The panel can disencumber the $25,000 and re-encumber it for another project beginning in 1996-97. When the panel disencumbers and then re-encumbers funds, it is able to extend the length of time it uses the appropriation. In the above example, the panel and its contractors should have used the $100,000 originally encumbered in fiscal year 1994-95 by the end of fiscal year 1996-97. However, the $25,000 it disencumbered and immediately re-encumbered in 1996-97 will now be available for an additional three-year period ending fiscal year 1998-99. Figure 3 shows that, by disencumbering the $25,000 and then immediately re-encumbering those same funds, the panel is able to extend from three to five years the length of time the funds are available.

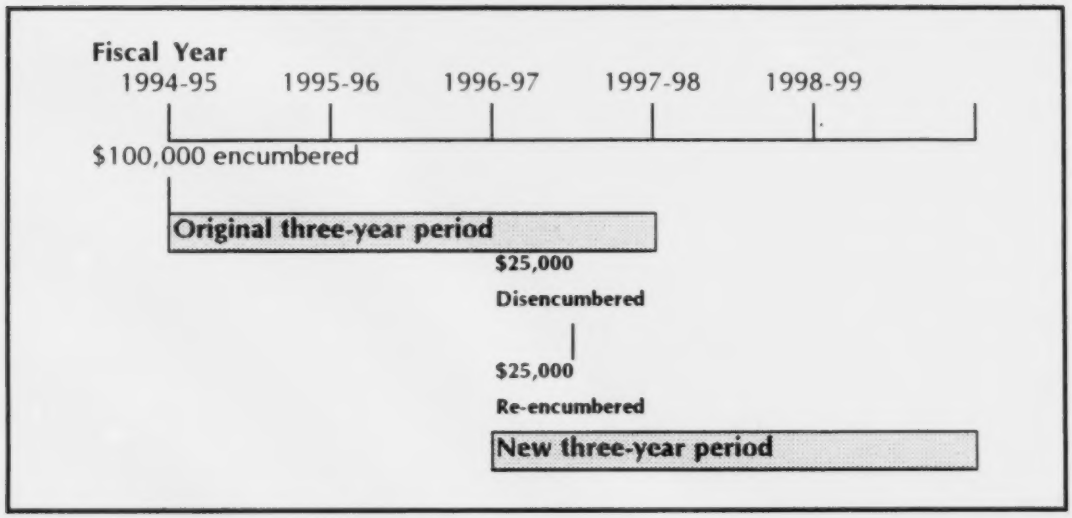
We also found that the panel is using this budget act provision to prolong the availability of funds encumbered to particular contracts. Specifically, near the end of each fiscal year, the panel analyzes contracts appropriated with funds that will revert to the Unemployment Insurance Fund due to the three-year time limit. The panel disencumbers these funds and then immediately re-encumbers them to the same contract. It is thus able to change the appropriation identity of the funds to the current year, thereby extending the amount of time they are available to the panel. In fiscal year 1995-96, the panel used this provision to extend the availability of $15.4 million from the fiscal year 1993-94 appropriation.

No panel funds have ever reverted to the Unemployment Insurance Fund.

The statutes are not clear as to whether the Legislature, when it included this provision in the budget act, intended the panel to have the authority to perform these actions. However, by giving it this authority, the Legislature has allowed the panel to prolong the life of its funds indefinitely. In fact, no funds have ever reverted to the Unemployment Insurance Fund. The practice of disencumbering and re-encumbering funds is an inefficient process, whether it results from unsuccessful training projects or efforts to prolong the appropriated life of funding. To a certain extent, the panel cannot control the unsuccessful completion of a contract. However, to disencumber funds to extend the life of appropriations appears improper and should be discontinued.

Figure 3

The Panel's Ability To Extend Length of Appropriation



The Panel May Be Spending More Administrative Funds Than Intended

The panel is able to exceed its 15 percent administrative cost cap by charging unspent prior-year funds again in subsequent years.

The practice it employs to prolong the life of its funds may also lead to the panel exceeding the amounts allowed for administration. Section 10206(a)(2) of the Unemployment Insurance Code states that the panel's administrative costs shall not exceed 15 percent of the amount annually available for expenditure excluding expenses related to marketing, research, and evaluations. The annual budget act determines how much will be available to the panel for expenditure. However, as noted in the previous section, when the panel disencumbers and re-encumbers funds, it is able to change their fiscal year identity. When this happens, funds disencumbered from prior years' appropriations are included as amounts available for expenditure in the current fiscal year. Therefore, the panel is able to spend on administration up to 15 percent of the funds appropriated by the Legislature for a fiscal year plus up to 15 percent of those funds disencumbered from prior fiscal years. The panel is thus able to use more than 15 percent of the funds appropriated to it for administrative expenses.

For example, in fiscal year 1994-95, the panel spent $9.1 million, only 10.5 percent of the $86.9 million funds available to it that year, on administration. However, disencumbrances comprised $45.2 million of the $86.9 million.

If we do not include disencumbrances, which were funds originally appropriated in a prior fiscal year, when calculating the amount the panel used for administrative expenses, the percentage would be 21.8 percent rather than 10.5 percent. Because the panel can control to a certain extent the amount of funds it disencumbers, it is able to influence, outside the purview of the Legislature, the amount it can spend on administration.

The Panel Encumbered Funds Inappropriately

Although it committed $7 million for a contract, the panel never intended for the contractor to provide training services.

During our review of its contracting process, we became aware of a contract the panel made with the California Manufacturers Association (CMA) that set aside funds for a specific group. In fiscal year 1993-94, the panel entered into a training contract for $7 million with the CMA. Accordingly, the panel encumbered $7 million of fiscal year 1993-94 funds for the contract. However, it never intended the CMA to provide training services. Rather, its responsibilities under the contract included marketing the panel program to the CMA membership, developing projects, providing technical assistance to interested companies, and administering projects approved by the eight-member panel. Effectively, the panel earmarked $7 million in training funds for CMA members by encumbering these funds in the CMA contract that did not involve training services.

The State Administrative Manual, Section 1205, states that a contract will be comprised of the following elements:

- A clear and accurate identification of the parties;
- The time for performance or completion of the contract;
- Amount to be paid; and
- A clear and complete statement of the work, service, or product to be performed, rendered, or provided.

The panel's contract with the CMA does not fulfill these requirements. As stated above, the panel never intended the CMA to provide training services. In addition, it has not paid any funds to the CMA; rather, when a company affiliated with the CMA received approval for a training project, the panel funded the project using current-year funds and then

disencumbered the same amount from the CMA contract. According to the executive director, the panel does not plan to enter into any additional contracts that are similar.

We also noted that, at June 30, 1996, the panel had $3.9 million remaining encumbered but unused on the CMA contract even though the contract had expired on December 31, 1995. The executive director stated that the panel retained the $3.9 million encumbrance in April 1996. This was done to maintain funding for projects being considered by the CMA prior to the end of the fiscal year. However, the panel was not able to provide us a list of these projects. In August 1996, after we raised concerns about the contract, the panel disencumbered the remaining $3.9 million.

Because of the inappropriate contract, $1 million in training contracts were delayed and $2.9 million was not reverted to the Unemployment Insurance Fund.

The Unemployment Insurance Code, Section 1611(b), states that any moneys allocated to the panel in a fiscal year and not encumbered in that fiscal year shall revert to the Unemployment Insurance Fund. Because the panel's contract with the CMA did not involve training services, the funds should not have been encumbered. At June 30, 1996, the panel had $1.0 million in contracts approved but not funded because it had run out of money. If the panel had not retained the $3.9 million on the CMA contract after the contract had expired, it could have avoided a delay in funding the $1.0 million in contracts on its waiting list. Moreover, because it did not have any other approved contract waiting, the remaining $2.9 million would have reverted to the Unemployment Insurance Fund. Finally, by processing a contract for services it never intended to pay for or receive, the panel wasted the time and resources of its staff members, and the staff at the Employment Development Department who handle the panel's accounting function.

Conclusion

The panel is accomplishing many of its responsibilities in both its program and administrative areas. However, it could improve its strategic planning efforts by stating its goals and objectives in measurable terms, and its units could better measure progress towards meeting those goals and objectives if they established performance benchmarks. In addition, the panel could be more effective and efficient in the way it delivers training funds to eligible California companies. Specifically, the panel needs to develop better estimates of amounts it awards to contractors. In addition, it needs to better monitor the amount of training funds its contractors earn. In making these improvements, the panel can maximize the use of funds available and lower the rate of disencumbrances it incurs each

year. Finally, the panel has engaged in certain administrative practices that, although legal, appear to be improper, including extending the life of its appropriated funds, expending more than 15 percent of appropriated funds for a particular year on administration, and encumbering funds to a contract from which it received no training services.

Recommendations

To ensure that it is successful in achieving its stated goals and objectives and fulfilling its mission, the panel should do the following:

- State its organizational goals and objectives in measurable terms whenever possible.

- Establish performance benchmarks for its employees so it can measure their success and challenge their performance.

To reduce the amount of disencumbrances it incurs, the panel should take the following actions:

- Delineate in its annual report to the Legislature the effect the panel's implementation of recommendations from the disencumbrance report has had on the disencumbrance rate when these effects are measurable.

- If the changes it made as a result of the disencumbrance report are not effective in lowering the rate of disencumbrances, consider alternative means, such as using phased contracts, instituting a penalty on unsuccessful companies, or implementing other procedures suggested by the Advisory Research Council or the California State University, Northridge, study.

To ensure that the panel is spending its funds appropriately, the Legislature should do the following:

- Consider the methods by which the panel is allowed to extend the life of its appropriated funds, and if these methods are contrary to the intent of the Legislature, eliminate the budget act language that allows the panel to re-encumber funds.

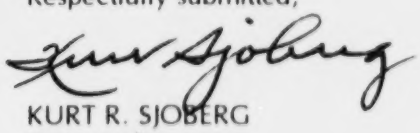
- Consider the methods employed by the panel to use more than 15 percent of appropriated funds for administration, and if those methods are contrary to the intent of the

Legislature, limit the panel to using only a certain percentage of each year's appropriation and excluding amounts disencumbered from prior fiscal year appropriations.

To be more effective in its operations, the panel should stop entering into contracts and encumbering training funds for which it does not intend to receive training services.

We conducted this review under the authority vested in the state auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope of this report.

Respectfully submitted,



KURT R. SJOBERG
State Auditor

Date: October 1, 1996

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ETP (2/96)

September 23, 1996

Kurt R. Sjoberg, State Auditor
Bureau of State Audits
660 J Street, Suite 300
Sacramento, CA 95814

Dear Mr. Sjoberg:

Thank you for the opportunity to review and respond to the audit of the Employment Training Panel (ETP) program conducted by the Bureau of State Audits, as required by Unemployment Insurance Code Section 10206.5. The Panel commends your staff for the thoroughness of their review and the manner in which they conducted this audit. We appreciate their courtesy in working with ETP staff and their professional approach in reviewing the Panel program. Their willingness to learn the details of our program is reflected in the clarity and quality of the final audit report. We read the report with interest and are happy to provide this response to it.

We are pleased the audit found the Panel is fulfilling it responsibilities in both program and administrative areas. The Panel will continue to ensure it fulfills these responsibilities in its role as a significant economic development tool for California. We will continue to work closely with other entities such as the Trade and Commerce Agency, educational institutions, other State departments and the Panel's Advisory Research Council, and through ETP staff quality improvement teams, to ensure continuous program improvement.

Generally, we concur with the findings submitted in the audit report. We agree that improvements can be made in several areas identified in the report. At the same time, many of these issues had also been identified by Panel staff and work is underway to make the identified improvements. The following provides our response to the specific findings of the audit report.

Finding: The Panel Is Accomplishing Many of Its Responsibilities, but Can Improve Its Strategic Planning Process

Response: Again, we are pleased the audit found the Panel is achieving its overall mission through the appropriate application of its contracting procedures, program audits, fiscal processes, administrative procedures, and electronic data processing systems. We will continue to strive for excellence in these areas as we work with our many economic development partners to assure California businesses and workers are able to compete successfully in the global economy.

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We recognize the need to set measurable objectives where possible in the Panel's strategic planning process so the success of the program can be measured and continuous improvements can be made. At the same time, we feel the Plan, as written, meets the overall purpose of an ETP strategic plan as provided in the ETP legislation, and we believe it appropriately sets forth the Panel's strategies and goals for accomplishing its mission. The Plan clearly delineates the Panel's strategies for working in concert with entities such as the Economic Strategy Panel, educational institutions, other State agencies, and ETP's Advisory Research Council to ensure skilled workers for California businesses in support of the State's overall economy.

In effect, the Plan is built upon several implicit measures which ensure the Panel is able to continually evaluate the success of its program. ETP is unique in that its performance-based contracting requirement provides an inherent benchmark for measuring the success of the program at all times -- i.e., a measure of success is provided automatically through an assessment of the number of trainees who complete Panel-funded training and the required retention period, vis-vis the cost of providing this training. The Plan is framed with the overall intent of continually improving the program's ability to best meet these basic objectives.

The Plan also sets forth the Panel's research agenda for assuring ETP is meeting its objectives and fulfilling its mission, and to ensure the Panel addresses the State's future economic needs. Here, a recent longitudinal study conducted by California State University, Northridge found ETP training has resulted in increased earnings and employment security for trainees, even three years after the completion of training and ETP training generated an annual return of up to more than five times the original investment.

We feel the nature of performance-based contracting and ongoing program research and evaluation provide the Panel with effective means for determining the success of the program. At the same time, we agree that additional measurable objectives should be developed so the Panel can better state its organizational goals and establish benchmarks for its employees to achieve those goals. Therefore, where possible, we will include more measurable objectives in the Panel's Three-Year Strategic Plan.

However, given the primary audience for the Three-Year Plan are the Governor and Legislature, we feel it is inappropriate for the Plan to include goals and objectives which are too detailed. Rather, such goals and objectives are more appropriately the function of an internal plan for implementing the broaderer strategies and objectives stated in the Three-Year Plan. Therefore, I have instructed the Panel's Executive Director to develop such an implementation plan with detailed goals and objectives by the end of the 1996 calendar year. This plan will be updated on an annual basis as an ongoing means of implementing the Three-Year Strategic Plan.

<u>Finding: The Panel Needs to Better Manage Its Distribution of Funds</u>

a. The Panel Needs to Better Estimate the Amount of Funds Contractors Will Earn

Response: Since its inception ETP has been a 100 percent performance-based contracting program,

which ensures that the training is tied to a real job. This means no funds are earned by a contractor until a trainee completes all of the training and a subsequent employment retention period of at least 90 days in a training-related job at a stipulated wage. The previously referenced three-year longitudinal study also found, in terms of increased worker earnings, the Panel's unique performance-based contracting produces outcomes similar to those found for training which is purely private. Researchers found this level of efficiency is unusual in a publicly funded training program.

Further, ETP is an employer driven program. Businesses identify their own training needs and the Panel works directly with those businesses to help them meet those needs. Ideally, a successful contract would accomplish all training as planned, with a contractor earning all of the encumbered funds. However, with a 100 percent performance-based contracting program, and with circumstances often beyond the contractor's control, some fund disencumbrances will occur in most cases.

With this in mind, the Panel has implemented a number of policies and procedures to increase the potential for successful contracts. During the development phase of the ETP contracting process, Panel development staff work with contractors to identify and reduce factors which could subject the training project to greater risk of failure. Panel monitoring staff also work to identify any problems at the early stages of projects so that actions can be taken to correct the problems or terminate the contract and disencumber the funds. In addition, throughout the term of the agreement the monitoring analysts continually assess the need for amendments to disencumber funds that will not be earned.

b. By Revising its Contract Management Practices, the Panel Could Serve Employers Sooner

Response: The Panel has taken action on the recommendations of its internal disencumbrance study, by implementing policy and procedures for its staff. It will be some time before the effect of implementing the new policies and procedures can be measured. However, the Panel will evaluate the effect of these actions on reducing disencumbrances and report the results of the evaluation to the California Legislature in its annual report. It will also report the results and findings from the California State University, Northridge study on the role of consultants in ETP contracts in the annual report.

The Panel has taken the following action on the remaining two recommendations from the Disencumbrance Study:

- To encourage contractors to plan their projects more realistically the Panel has implemented procedures to allow contractors to amend agreements to add funds at a later date without being required to make a substantial contribution.

- To strengthen a contractor's understanding of ETP's contractual requirements and their commitment to implement a successful training contract the Panel has also implemented a policy requiring an operational senior management representative participate in an initial site visit meeting conducted prior to contract development.

c. The Panel Could Adopt Policies to Deter Contractors from Overstating Their Funding Needs

Response: The Panel will consider the possibility of penalizing contractors who don't successfully complete their training agreements, if necessary, after its careful and thorough evaluation of the effect the new policies and procedures have had on reducing disencumbrances.

Finding: Some Panel Fiscal Practices May Not Be Appropriate

Response: The audit report questioned the appropriateness of the Panel's ability to change prior-year appropriated funds into current-year funds, thereby extending the length of time the funds are available (e.g., from three to five years.) We feel Budget language clearly allows the Panel to extend the life of budget appropriations and prolong the availability of funds encumbered to particular contracts. Language in the Budget Act, Chapter 162, 5100-001-0514, Provision 1, states "funds disencumbered from the Employment Training Funds training contracts ... are hereby appropriated for transfer to and in augmentation of, this item for allocation by the Employment Training Panel for training contracts".

However, we would point out the disencumbrance and re-encumbrance of funds of projects which have not completed occur only when it has been determined by Panel staff that the contractor in question will earn additional monies, but will not be able to invoice for those earnings until after the end of the fiscal year. Such delays in invoicing may be caused by :

- the term of the contract not ending until the end of the fiscal year (i.e., late June), with closeout not due until 30 days after the end of the term (automatically carrying over into the next fiscal year); or

- pending appeals submitted for trainees denied payment because of performance which was not met.

Based on the fact the Panel's training programs are performance based and most of ETP's contracts are written for a two-year term, it is virtually impossible to control the level of success of contract completion. ETP enters into agreements with contractors with the assumption each contractor will provide the training the contractor has requested during the development of the contract, and all funds encumbered will be earned. Due to a variety of unforeseen circumstances related to the contractor's business conditions, such as changes in the training needs, changes in production demand and equipment, employee layoffs, and inability of the employer to release employees for training, the amount actually earned by the contractor can differ greatly from the planned amount. Because of these factors, the Panel cannot control the amount of disencumbrances which can occur. However, the Panel has taken steps to help contractors improve their planning for achievable training, and to identify and reduce certain risk factors which can lead to higher disencumbrances.

Finding: The Panel May Be Spending More Administrative Funds Than Intended

Response: The audit report stated that the Panel may be spending more administrative funds than intended. It states because the UI code includes prior year disencumbrances in the amount annually available for expenditure, the Panel is able to influence the amount it can spend on administration. However, it is our view the Panel is spending the appropriate amount of funds on program administration and that amount is necessary to provide the needed administrative support for the associated training projects.

Unemployment Insurance Code Section 10206, (a) (2) states "The panel's administrative costs..., shall not exceed 15 percent of the amount annually available for expenditure by the panel". It is Panel's interpretation the "amount annually available for expenditure" includes monies disencumbered from prior years. This seems to be confirmed by the fact such funds must be "available for expenditure", since they are approved for and encumbered in training contracts during the year in question. Further, EDD which is responsible for administrating ETP's budget, holds this same view. According to the Panel's EDD budget analyst, it is also EDD's interpretation that prior year disencumbrances are factored into the amount annually available.

Further, we feel it is critical the annual 15 percent administrative funding amount be based upon this interpretation. These administrative funds are in direct support of the funds expended for training projects during the same fiscal year. All contracts approved during a fiscal year have associated administrative costs which are distributed over the lifetime of a contract. These include costs for project development, contract processing, monitoring and technical assistance, fiscal support, project close-out and auditing.

Finding: The Panel Encumbered Funds Inappropriately

Response: The Panel concurs with the auditor's finding, but would like to explain the intent of the Panel at the time it entered into the master agreement with the California Manufacturers Association (CMA).

CMA's membership is made up of more than 800 major California manufacturers and food processors whose employees constitute over 70 percent of the industrial workforce in the state. The intent of the Panel was to serve the CMA membership by ensuring training funds would be available to retrain their current workers, or train new employees of companies expanding in or relocating to California. The resulting training agreements with the CMA membership did meet ETP statutory, regulatory and policy requirements.

The Panel agrees with the auditor's recommendation, and will not encumber funds for, or enter into agreements with contractors who do not intend to provide training services.

In conclusion, we appreciate the opportunity to review the audit report and provide this response. While we recognize improvements can be made as identified by the audit and covered in our response, we are pleased the audit found the Panel is fulfilling its program and administrative responsibilities. Again, we commend your staff for the professional manner in which they conducted the audit and for the quality of the final report.

If you have any questions or would like to discuss these comments, please contact Gerald Geismar, ETP's Executive Director, at (916) 327-5246.

Sincerely,

Thomas C. Ellick, Chairman

cc: Gerald G. Geismar

cc: Members of the Legislature
Office of the Lieutenant Governor
Attorney General
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps